Grant Thornton

Consolidated Financial Statements and Report of Independent Certified Public Accountants

Goodwill Industries of Southeastern Wisconsin, Inc. and Affiliates

December 31, 2016 and 2015

Contents

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

Board of Directors
Goodwill Industries of Southeastern Wisconsin, Inc. and Affiliates

Report on the financial statements

We have audited the accompanying consolidated financial statements of Goodwill Industries of Southeastern Wisconsin, Inc. (a Wisconsin non-stock, not-for-profit organization) and Affiliates (collectively, Goodwill), which comprise the consolidated statements of financial position as of December 31, 2016 and 2015, and the related consolidated statements of activities, operating expenses and cash flows for the years then ended, and the related notes to the financial statements.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to Goodwill's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Goodwill's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Goodwill Industries of Southeastern Wisconsin, Inc. and Affiliates as of December 31, 2016 and 2015, and the changes in their net assets and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Grant Thornton LLP

Appleton, Wisconsin
June 14, 2017

Goodwill Industries of Southeastern Wisconsin, Inc. and Affiliates
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
December 31,
(In thousands)

ASSETS	2016	2015
Cash and cash equivalents	$ 28,657	$ 22,785
Accounts receivable, net	11,503	12,383
Inventories and supplies, net	11,614	10,878
Prepaid expenses and other assets	2,832	2,828
Total current assets	54,606	48,874
Property, plant and equipment, net	155,433	158,972
Investments, other	550	465
Other long-term assets	25	118
TOTAL ASSETS	$210,614	$208,429

LIABILITIES AND NET ASSETS		
Liabilities		
Current maturities of long-term debt and capital leases	$ 3,383	$ 3,184
Accounts payable	9,153	11,058
Accrued liabilities	17,949	17,717
Deferred income	472	378
Total current liabilities	30,957	32,337
Long-term debt, less current maturities and bond issuance costs	43,863	46,373
Obligations under capital leases, less current maturities	1,551	1,705
Other long-term liabilities	2,202	2,636
Total liabilities	78,573	83,051
Net assets		
Unrestricted	131,541	125,072
Temporarily restricted	500	306
Total net assets	132,041	125,378
TOTAL LIABILITIES AND NET ASSETS	$210,614	$208,429

The accompanying notes are an integral part of these statements.

Goodwill Industries of Southeastern Wisconsin, Inc. and Affiliates
CONSOLIDATED STATEMENT OF ACTIVITIES
Year ended December 31, 2016
(In thousands)

	Unrestricted	Temporarily restricted	Total
Operating revenue and support			
Retail services	$152,841	$ -	$152,841
Retail in-kind services	99,041	-	99,041
Great Lakes Naval Base services	70,165	-	70,165
Participant programs and services	41,356	-	41,356
Manufacturing services	26,006	-	26,006
Total operating revenue	389,409	-	389,409
Contributions	1,027	608	1,635
Miscellaneous revenue	1,565	-	1,565
Net assets released from restrictions	414	(414)	-
Total operating revenue and support and net assets released from restrictions	392,415	194	392,609
Operating expenses			
Program services	360,897	-	360,897
Management and general	24,507	-	24,507
Fundraising	761	-	761
Total operating expenses	386,165	-	386,165
Excess of operating revenue and support and net assets released from restrictions over operating expenses	6,250	194	6,444
Income tax expense	125	-	125
Non-operating activities			
Gain on disposal of property, plant and equipment, net	344	-	344
Change in net assets	6,469	194	6,663
Net assets, beginning of year	125,072	306	125,378
Net assets, end of year	$131,541	$ 500	$132,041

The accompanying notes are an integral part of this statement.

Goodwill Industries of Southeastern Wisconsin, Inc. and Affiliates
CONSOLIDATED STATEMENT OF ACTIVITIES
Year ended December 31, 2015
(In thousands)

	Unrestricted	Temporarily restricted	Total
Operating revenue and support			
Retail services	$147,719	$ -	$147,719
Retail in-kind services	95,682	-	95,682
Great Lakes Naval Base services	74,431	-	74,431
Participant programs and services	45,982	-	45,982
Manufacturing services	28,100	-	28,100
Total operating revenue	391,914	-	391,914
Contributions	1,704	320	2,024
Miscellaneous revenue	1,534	-	1,534
Net assets released from restrictions	346	(346)	-
Total operating revenue and support and net assets released from restrictions	395,498	(26)	395,472
Operating expenses			
Program services	360,375	-	360,375
Management and general	24,200	-	24,200
Fundraising	743	-	743
Total operating expenses	385,318	-	385,318
Excess (deficiency) of operating revenue and support and net assets released from restrictions over operating expenses	10,180	(26)	10,154
Non-operating activities			
Gain on disposal of property, plant and equipment, net	64	-	64
Change in net assets	10,244	(26)	10,218
Net assets, beginning of year	114,828	332	115,160
Net assets, end of year	$125,072	$ 306	$125,378

The accompanying notes are an integral part of this statement.

Goodwill Industries of Southeastern Wisconsin, Inc. and Affiliates
CONSOLIDATED STATEMENT OF OPERATING EXPENSES
Year ended December 31, 2016
(In thousands)

	Program services	Management and general	Fundraising	Total
Salaries	$116,533	$12,418	$266	$129,217
Employee benefits	23,061	2,363	38	25,462
Payroll taxes	9,993	846	17	10,856
Total salaries and related expenses	149,587	15,627	321	165,535
Retail in-kind supplies	98,753	-	-	98,753
Supplies and other	58,079	190	15	58,284
Rent and occupancy	22,482	605	9	23,096
Professional fees and contracted services	10,329	3,159	227	13,715
Depreciation	12,582	769	-	13,351
Advertising	2,503	1,765	-	4,268
Transportation	3,019	215	-	3,234
Equipment purchases, rental and maintenance	2,833	1,097	125	4,055
Interest expense	32	765	-	797
Conferences and training	252	315	58	625
Specific assistance to individuals	440	-	-	440
Bad debt expense, net	6	-	6	12
Total expenses	$360,897	$24,507	$761	$386,165

The accompanying notes are an integral part of this statement.

Goodwill Industries of Southeastern Wisconsin, Inc. and Affiliates
CONSOLIDATED STATEMENT OF OPERATING EXPENSES
Year ended December 31, 2015
(In thousands)

	Program services	Management and general	Fundraising	Total
Salaries	$116,385	$11,619	$288	$128,292
Employee benefits	22,394	2,098	40	24,532
Payroll taxes	10,575	792	18	11,385
Total salaries and related expenses	149,354	14,509	346	164,209
Retail in-kind supplies	94,937	-	-	94,937
Supplies and other	63,296	230	27	63,553
Rent and occupancy	21,364	516	17	21,897
Professional fees and contracted services	10,403	4,396	254	15,053
Depreciation	11,931	732	-	12,663
Advertising	2,339	1,214	-	3,553
Transportation	3,066	224	2	3,292
Equipment purchases, rental and maintenance	2,924	987	46	3,957
Interest expense	36	1,078	-	1,114
Conferences and training	295	314	51	660
Specific assistance to individuals	406	-	-	406
Bad debt expense, net	24	-	-	24
Total expenses	$360,375	$24,200	$743	$385,318

The accompanying notes are an integral part of this statement.

Goodwill Industries of Southeastern Wisconsin, Inc. and Affiliates
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years ended December 31,
(In thousands)

	2016	2015
Cash flows from operating activities		
Change in net assets	$ 6,663	$ 10,218
Adjustments to reconcile change in net assets to net cash provided by operating activities		
Depreciation and amortization	13,375	12,681
Realized and unrealized loss (gain) on investments	(46)	39
Loss on write-off of bond issuance costs	-	29
Unrealized (gain) loss on interest rate swaps	(526)	(55)
Gain on disposal of property, plant and equipment, net	(344)	(64)
Accounts receivable allowance	(8)	-
Changes in operating assets and liabilities		
Accounts receivable	888	(1,024)
Inventories and supplies	(736)	(1,080)
Prepaid expenses and other assets	(4)	408
Accounts payable and accrued liabilities	(1,673)	(3,293)
Deferred income	94	(853)
Other long-term assets and liabilities	205	20
Net cash provided by operating activities	17,888	17,026
Cash flows from investing activities		
Capital expenditures	(9,881)	(21,748)
Proceeds from sale of property, plant and equipment	828	64
Purchases of investments	(59)	(59)
Net cash used in investing activities	(9,112)	(21,743)
Cash flows from financing activities		
Issuance of long-term debt	294	10,818
Repayment of long-term debt	(2,708)	(3,490)
Payments under capital lease obligations	(490)	(381)
Net cash (used in) provided by financing activities	(2,904)	6,947
Net increase in cash and cash equivalents	5,872	2,230
Cash and cash equivalents, beginning of year	22,785	20,555
Cash and cash equivalents, end of year	$28,657	$ 22,785
Supplemental disclosure of cash flow information		
Cash payments for interest	$ 1,315	$ 1,289
Non-cash transactions		
Capitalized interest	$ 38	$ 234
Purchases of property and equipment financed through capital leases	414	1,639
Donated goods and materials contributed for resale	99,041	95,682

The accompanying notes are an integral part of these statements.

NOTE A - ORGANIZATION

Goodwill Industries of Southeastern Wisconsin, Inc. and Affiliates (collectively, Goodwill) was formed in 1919 and is a Wisconsin non-stock, not-for-profit corporation. The mission of Goodwill is to provide training, employment and supportive services for people with disabilities or disadvantages who seek greater independence. Disabilities or disadvantages include physical or intellectual disabilities, mental health issues, skill limitations, lack of education and job preparation, communication challenges and other socio-economic disadvantages.

Goodwill pursues its mission by employing people with disabilities and other barriers within the organization's own operations in southeastern Wisconsin and northeastern Illinois. In addition, Goodwill provides social services, community programs, workforce development, transitional employment, employment services and supportive services for individuals who have disabilities, are disadvantaged or have other special needs, in order to enhance their employment opportunities, prevent or alleviate rehabilitation problems and facilitate their ability to live independently in the community.

Goodwill Industries of Southeastern Wisconsin, Inc. has the following affiliates and subsidiaries: Goodwill Industries of Metropolitan Chicago, Inc. is a separate, not-for-profit entity that focuses on providing mission services in the Metropolitan Chicago area. Goodwill Retail Services, Inc. is a separate, not-for-profit entity responsible for the retail stores operated by Goodwill. Goodwill Manufacturing, Inc. is a separate, for-profit corporation that provides assembly and packaging services. On March 24, 2016, Goodwill Manufacturing, Inc. changed its name to GWMFG, Inc. All outstanding shares of GWMFG, Inc. common stock are held by Goodwill Industries of Southeastern Wisconsin, Inc. Goodwill TalentBridge, LLC is a separate limited liability company that provides customized staffing solutions. Goodwill Industries of Southeastern Wisconsin, Inc. is the sole member and manager of Goodwill TalentBridge, LLC. On February 11, 2015, Goodwill Work Solutions, Inc. was created as a separate, not-for-profit entity. On March 24, 2016, Goodwill Work Solutions, Inc. changed its name to Goodwill Manufacturing, Inc. Effective December 31, 2016, GWMFG, Inc. was dissolved into Goodwill Industries of Southeastern Wisconsin, Inc., and Goodwill Industries of Southeastern Wisconsin, Inc. contributed the assets and liabilities of GWMFG, Inc. to Goodwill Manufacturing, Inc.

NOTE B - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies used by Goodwill is as follows:

Financial Statement Presentation

The consolidated financial statements are prepared on the accrual basis of accounting. All significant intercompany activity has been eliminated.

Net assets, revenues, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. This has been accomplished by classification of net assets and transactions as unrestricted or temporarily restricted, as follows:

<u>Unrestricted Net Assets</u>

Net assets and transactions are not subject to donor-imposed stipulations.

Temporarily Restricted Net Assets

Net assets and transactions are subject to donor-imposed stipulations that will be met by the actions of Goodwill and/or the passage of time. As of December 31, 2016 and 2015, Goodwill has $500 and $306, respectively, of net assets restricted by donors for specific programs.

Contribution revenue is reported as an increase in unrestricted net assets unless use of the related assets is limited by donor-imposed restrictions. Restricted contributions whose purpose has been fulfilled and/or the stipulated time period has elapsed are reported as reclassifications between temporarily restricted and unrestricted net assets.

Contributions

All contributions are considered to be available for general operating purposes unless specifically restricted by the donor. Contributions, including unconditional promises to give, are recognized as revenue in the period received. Conditional promises to give are not recognized until the conditions on which they depend are substantially met. Contributions to be received after one year are discounted at an appropriate discount rate commensurate with the risks involved. Amortization of the discount is recorded as additional contribution revenue and classified in accordance with donor-imposed restrictions on the contributions. An allowance for uncollectible contributions receivable is provided based on management's judgment and consideration of such factors as prior collection history, type of contributions and nature of fundraising activity.

In-kind Contributions

Goods and materials contributed to Goodwill for resale are recorded at estimated fair market value based on retail sales prices. Costs associated with refurbishing these goods and materials are charged to expense as incurred.

In-kind contributions and grants received for goods or services are recorded at estimated fair value at the date of donation.

Government Contracts

Service contracts are received from various federal, state and local governments, governmental agencies and other not-for-profit organizations. These programs are considered exchange transactions and are therefore recorded as unrestricted revenue. Expenditures of government service contract funds are for the purposes specified by the funding source.

Revenue Recognition

Goodwill recognizes revenue from commercial contracts in the period service is provided or goods are shipped. Revenue from the sale of goods received as in-kind contributions is recorded as unrestricted revenue in the period the sale is made. Revenue from government contracts is recognized when allowable and reimbursable expenditures are incurred, and upon meeting the legal or contractual requirements of the funding source.

Cash and Cash Equivalents

Goodwill considers all highly liquid investments with original maturities of three months or less to be cash equivalents.

Goodwill maintains its cash balances in three financial institutions, which at times may exceed federally insured limits. Goodwill has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash and cash equivalents.

Investments

Goodwill reports investments at fair value, with net appreciation and depreciation reported in the consolidated statements of activities.

Goodwill's investments are exposed to various risks, such as interest rate, market and credit risks. Due to the level of risk associated with certain investments and the level of uncertainty related to changes in the values of investments, it is at least reasonably possible that changes in risk in the near term could materially affect Goodwill's investment holdings.

Investments, other are designated and intended for the use of satisfying the liabilities of the 457(b) plan, as described in note K.

Accounts Receivable

The majority of Goodwill's accounts receivable is due from companies in the manufacturing industry and from government agencies. Credit is extended based on an evaluation of a customer's financial condition and, generally, collateral is not required. Accounts receivable are due within 10 to 30 days and are stated as amounts due from customers net of an allowance for doubtful accounts. Accounts outstanding longer than the contractual payment terms are considered past due. Goodwill determines its allowance by considering a number of factors, including the length of time accounts receivable are past due, Goodwill's previous loss history, the customer's current ability to pay its obligation to Goodwill, and the condition of the general economy and the industry as a whole. Total allowances for uncollectible balances was $372 and $380 as of December 31, 2016 and 2015, respectively. Goodwill writes off accounts receivable when they become uncollectible, and payments subsequently received on such receivables are credited to the allowance for doubtful accounts.

Inventories and Supplies

Inventories primarily represent merchandise held for resale and component manufacturing supplies. In-kind contributions of merchandise inventory held for resale are recorded at estimated fair market value based on retail sales prices. Component manufacturing supply inventory is recorded at the lower of cost or market determined on a first-in, first-out basis.

Property, Plant and Equipment

Purchases of property, plant and equipment are recorded at cost. Donated assets are capitalized at estimated fair value when received. Leased property under capital leases is capitalized at the lesser of the useful life of the leased asset or the term of the lease. Goodwill capitalizes all qualifying purchases over $5. Depreciation and amortization are provided using the straight-line method over the estimated useful lives of the assets ranging as follows: land improvements from 3 to 15 years; buildings and improvements from 3 to 50 years; and equipment and vehicles from 3 to 15 years. Leased assets are depreciated using the straight-line method over the lesser of the lease term or the estimated useful lives of the assets ranging from 3 to 15 years. Amortization of assets held under capital leases is included in depreciation expense.

Bond Issuance Costs

Bond issuance costs represent trust fees, legal fees and other costs associated with the various bond issuances, and are netted against long-term debt on the consolidated statements of financial position. These costs are amortized over the life of the bonds (11 to 25 years). In 2015, $29 of existing costs, net of accumulated amortization, were written off in association with the 1999 bonds, which were paid off during 2015 using proceeds from a bank note payable. Accumulated amortization was $25 and $39 as of December 31, 2016 and 2015, respectively.

Deferred Income

Deferred income consists of funds received in advance of providing services and supplies related to certain government service contracts. The majority of the balance as of December 31, 2016 and 2015, relates to a significant contract with a branch of the U.S. government.

Cost Allocation

Expenses by function have been allocated between program, management and general, and fundraising classifications on the basis of actual expenditures, square footage, time records and estimates made by management.

Advertising

Goodwill expenses the cost of advertising as incurred. Advertising expense for the years ended December 31, 2016 and 2015, was $4,268 and $3,553, respectively.

Income Taxes

Goodwill Industries of Southeastern Wisconsin, Inc., Goodwill Industries of Metropolitan Chicago, Inc., Goodwill Retail Services, Inc. and Goodwill Manufacturing, Inc. have received determination letters from the Internal Revenue Service (IRS) indicating that they are exempt from federal income taxes, except for taxes pertaining to unrelated business income under section 501(c)(3) of the Internal Revenue Code. See note I for the GWMFG, Inc. income tax disclosure.

Goodwill TalentBridge, LLC has been organized as a limited liability company and, accordingly, is not subject to federal or state income taxes. All income tax attributes of the entity are passed through to its sole member, Goodwill Industries of Southeastern Wisconsin, Inc. The entity is included in the consolidated information return filed by Goodwill Industries of Southeastern Wisconsin, Inc.

The Financial Accounting Standards Board (FASB) issued guidance related to the uncertainty of income tax positions, which clarifies the accounting for uncertainty in income taxes recognized in an organization's financial statements and requires additional disclosure. Goodwill recognizes the financial statement benefit of a tax position only after determining that the relevant tax authority would more likely than not sustain the position following an audit. For tax positions meeting the more likely than not threshold, the amount recognized in the financial statements is the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the relevant tax authority.

Goodwill files information returns in the U.S. federal and the states of Wisconsin and Illinois jurisdictions. Tax years open under the federal statute of limitations include 2013 through 2016. Tax years open under the state of Wisconsin and state of Illinois statutes include 2012 through 2016.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain reclassifications have been made to the 2015 amounts to conform to the 2016 presentation. There was no effect on net assets or change in net assets as previously reported.

New Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09) as a new Topic, Accounting Standards Codification *Topic 606.* The amendments are intended to provide a more robust framework for addressing revenue issues, improve comparability of revenue recognition practices and improve disclosure requirements. In August 2015, the FASB issued ASU No. 2015-14, *Revenue from Contracts with Customers: Deferral of the Effective Date*, which deferred the effective date of ASU 2014-09 by one year. This ASU is effective for annual reporting periods beginning after December 15, 2017, and shall be applied using either a full retrospective or modified retrospective approach. Early adoption is permitted. The new guidance is effective for Goodwill in 2018. Goodwill is currently evaluating the impact on the results of operations, financial condition and cash flows and has not determined the impact on its consolidated financial statements at this time.

In April 2015, the FASB issued ASU No. 2015-03, *Simplifying the Presentation of Debt Issuance Costs*, which requires entities to present debt issuance costs related to recognized debt liability as a direct deduction from the carrying amount of the debt liability. Goodwill adopted this guidance in 2016 and reclassified the 2015 bond issuance costs to confirm to the 2016 presentation.

In March 2016, the FASB issued ASU No. 2016-02, *Leases*, as a new topic, Accounting Standards Codification 842. The objective of ASU No. 2016-02 is to increase transparency and comparability among organizations by reorganizing lease assets and lease liabilities on the statement of financial position and disclosing key information about leasing arrangements. ASU No. 2016-02 is effective for annual reporting periods beginning after December 15, 2018, and shall be applied using either a full retrospective or modified retrospective approach. Early adoption is permitted. The new guidance is effective for Goodwill in 2019. Goodwill is currently evaluating the impact on the results of operations, financial condition and cash flows and has not determined the impact on its consolidated financial statements at this time.

(In thousands)

In August 2016, the FASB issued ASU No. 2016-14, *Presentation of Financial Statements of Not-For-Profit Entities*, which is intended to improve how a not-for-profit entity classifies its net assets, as well as the information it presents in its financial statements about liquidity and availability of resources, expenses and investment return, and cash flows. This ASU is effective for annual reporting periods beginning after December 15, 2017, and shall be applied retrospectively. Early adoption is permitted. The new guidance is effective for Goodwill in 2018. Goodwill is currently evaluating the impact on the results of operations, financial condition and cash flows, and has not determined the impact on its consolidated financial statements at this time.

NOTE C - INVENTORIES AND SUPPLIES

Inventories and supplies, net consists of the following as of December 31:

	2016	2015
Components	$ 2,389	$ 1,806
Retail merchandise	8,737	8,450
Food	395	487
Laundry	243	255
Gross inventory	11,764	10,998
Less reserve for excess and obsolete	(150)	(120)
Inventories and supplies, net	$11,614	$10,878

NOTE D - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment, net consists of the following as of December 31:

	2016	2015
Land	$ 32,903	$ 33,144
Land improvements	7,639	6,920
Building and improvements	170,338	163,169
Equipment and vehicles	50,307	46,689
Construction in process	1,312	4,138
Total property, plant and equipment	262,499	254,060
Less accumulated depreciation and amortization	(107,066)	(95,088)
Property, plant and equipment, net	$ 155,433	$158,972

(In thousands)

NOTE E - LINE-OF-CREDIT AGREEMENT

Goodwill has a working capital line-of-credit agreement with a bank, secured by substantially all assets, under which it may borrow up to $13,500 as of December 31, 2016. The agreement expires on May 31, 2018. Borrowings under the line-of-credit agreement bear interest at a variable rate (1.75% as of December 31, 2016). There was no outstanding balance as of December 31, 2016 and 2015. The line-of-credit agreement contains certain restrictive covenants which, among other things, require Goodwill to maintain certain financial ratios. Goodwill was in compliance with these covenants as of December 31, 2016 and 2015.

NOTE F - LONG-TERM DEBT

Long-term debt, payable by Goodwill, consists of the following as of December 31:

	2016	2015
WHEFA Revenue Bonds, Series 2014A, due in annual installments ranging from $540 to $840 through May 2029. The bonds bear interest, due monthly, at variable rates (1.33% at December 31, 2016). Collateralized by certain buildings.	$ 8,908	$ 9,464
WHEFA Revenue Bonds, Series 2014B, due in annual installments ranging from $135 to $210 through May 2029. The bonds bear interest, due monthly, at variable rates (1.33% at December 31, 2016). Collateralized by certain buildings.	2,227	2,366
WHEFA Revenue Bonds, Series 2014C, due in annual installments ranging from $570 to $1,210 through November 2035. The bonds bear interest, due monthly, at variable rates (1.33% at December 31, 2016). Collateralized by certain buildings.	16,429	17,000
WHEFA Revenue Bonds, Series 2014D, due in annual installments ranging from $475 to $735 through August 2025. The bonds bear interest, due monthly, at variable rates (1.39% at December 31, 2016). Collateralized by certain buildings.	5,595	6,090
WHEFA Revenue Bonds, Series 2012, due in annual installments ranging from $430 to $640 through February 2037. The bonds bear interest, due monthly, at variable rates (1.41% at December 31, 2016). Collateralized by certain buildings.	12,160	12,625
Notes payable to bank for various equipment loans, due in monthly installments ranging from $0.2 to $4. These notes bear interest, due monthly, at a fixed rate ranging from 4.45% to 4.50%.	287	-

(In thousands)

	2016	2015
Note payable to bank, due in annual installments of $475 each August 1 through 2019. The note bears interest, due monthly, at a fixed rate of 2.77%. Collateralized by certain buildings.	1,425	1,900
Total debt	47,031	49,445
Less current maturities	(2,820)	(2,701)
Less unamortized bond issuance costs	(348)	(371)
Long-term debt, less current maturities and unamortized bond issuance costs	$43,863	$46,373

During 2010, Goodwill entered into a guaranty agreement whereby provisions of the agreement provide that certain entities of the consolidated group are jointly liable for the outstanding debt of Goodwill Industries of Southeastern Wisconsin, Inc.

In an effort to reduce the risk of incurring higher interest costs in periods of rising interest rates, Goodwill is party to various interest rate swap agreements. The agreements effectively convert variable-rate debt to fixed-rate debt to the extent of the notional amount of the swaps. The interest differential is reflected as an adjustment to interest expense as incurred and the fair value of the swaps are reflected on the consolidated statements of financial position. The following is a summary of Goodwill's interest rate swaps at December 31:

Maturity date	Fixed rate	Total interest rate	Notional amount	Outstanding notional amount	Fair value liability 2016	Fair value liability 2015
July 1, 2019	3.15%	2.66%	$ 4,595	$ 1,130	$ (40)	$ (74)
May 1, 2019	2.39	1.90	15,000	11,138	(359)	(539)
May 2, 2022	(a)	(a)	8,940	8,940	(144)	(154)
December 1, 2022	2.54	2.13	6,000	5,403	(353)	(456)
December 1, 2022	1.32	0.90	2,100	1,893	(9)	(22)
January 14, 2024	1.97	1.56	2,600	2,424	(94)	(127)
December 2, 2024	2.24	1.80	7,500	6,986	(376)	(491)
December 1, 2024	1.85	1.42	3,500	3,260	(91)	(130)
					$(1,466)	$(1,993)

(a) There is no effective interest rate as of December 31, 2016, as interest payments begin on May 1, 2019.

The total increase in value of interest rate swaps recognized in interest expense (income) was $(527) and $(55) in 2016 and 2015, respectively.

The bonds payable contain certain restrictive covenants that, among other things, require Goodwill to maintain certain financial ratios. Goodwill was in compliance with these covenants as of December 31, 2016 and 2015.

(In thousands)

Aggregate scheduled principal payments on long-term debt and amortization expense of bond issuance costs as of December 31, 2016, are as follows:

	Long-term debt	Bond issuance costs
2017	$ 2,820	$ 25
2018	2,921	25
2019	3,007	25
2020	2,630	25
2021	2,734	25
Thereafter	32,919	223
	$47,031	$348

NOTE G - REFUNDABLE ADVANCES

Goodwill has entered into agreements with the Wisconsin Department of Transportation (DOT) to purchase certain vehicles for the transportation of its clients. The DOT funds 80% of the cost of the vehicles and Goodwill matches the remaining 20%. However, should Goodwill discontinue its transportation operations, the vehicles may be required to be returned to the DOT.

As of December 31, 2016, property, plant and equipment include $450 of assets and $264 of accumulated depreciation related to the vehicles. As of December 31, 2015, property, plant and equipment include $379 of assets and $178 of accumulated depreciation related to the vehicles. Goodwill has recorded a liability as of December 31, 2016 and 2015, of $185 and $178, respectively, which represents the portion of the costs funded by the DOT that would be required to be returned if the program ceased operations. This liability is recorded in other long-term liabilities on the accompanying consolidated statements of financial position.

NOTE H - LEASES

Goodwill is obligated under capital leases for certain equipment and vehicles that expire in October 2019. As of December 31, 2016 and 2015, property, plant and equipment include $3,906 and $3,740, respectively, of equipment under these capitalized leases and $1,986 and $1,750, respectively, of related accumulated depreciation and amortization.

Goodwill leases various retail and other operational facilities under non-cancelable operating lease agreements. Certain leases call for escalating rental payments. Goodwill also leases certain rehabilitation center facilities under leases that are cancelable only in the event that certain government funding ceases. These leases are considered non-cancelable for financial reporting purposes.

(In thousands)

As of December 31, 2016, future minimum lease payments under capital leases and non-cancelable operating leases were as follows:

	Capital leases	Operating leases
2017	$ 586	$10,307
2018	582	10,940
2019	499	10,215
2020	210	9,891
2021	124	9,189
Thereafter	160	38,492
Total minimum lease payments	2,161	$89,034
Less amounts representing interest	48	
Present value of net minimum lease payments	$2,113	

Total rental expense under all operating leases was $9,832 and $8,799 in 2016 and 2015, respectively.

Goodwill has certain cancelable lease rental agreements expiring in 2018. Total lease rental income was $183 and $174 in 2016 and 2015, respectively. Terms of cancellation include written notice 120 days prior to the effective date of termination. As of December 31, 2016, future minimum rental income under cancelable leases is as follows:

2017	$188
2018	106

NOTE I - INCOME TAXES

The deferred tax asset is a result of temporary differences between financial and income tax reporting for GWMFG, Inc., a for-profit entity. These temporary differences result primarily from various deferred tax assets that will be used to offset future taxable income. In assessing the deferred tax asset, management considers whether it is more likely than not that some, or all, of the deferred tax asset will not be realized. The ultimate realization of the deferred tax asset is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. As of December 31, 2016 and 2015, Goodwill's net deferred tax benefit was $-0-.

Goodwill classifies interest and penalties on underpayment of income taxes in the consolidated statement of activities as income tax (benefit) expense. There were no interest and penalties incurred and recorded for the years ended December 31, 2016 and 2015.

The current year tax expense is the result of GWMFG, Inc. transferring their remaining assets to Goodwill Manufacturing, Inc. at year-end.

NOTE J - SIGNIFICANT FUNDING AGENCIES AND CUSTOMERS

Goodwill has contracts with the US Naval Supply Systems Command to provide food, laundry and administrative services. The contracts expire on September 30, 2017. Goodwill recognized revenue of $70,165 and $74,431 in 2016 and 2015, or 23% and 24%, respectively, of operating revenue and support related to this customer. This customer accounted for $3,795 and $4,125, respectively, or 33% of the total accounts receivable balance as of December 31, 2016 and 2015.

Goodwill receives a substantial amount of funding from various federal and state agencies including the United States Department of Health and Human Services and the Wisconsin Department of Health and Family Services. Governmental grant awards are generally subject to renewal by grantor agencies on an annual basis.

A customer other than noted above accounted for $1,232 or 11%, of the total accounts receivable balance as of December 31, 2016.

NOTE K - EMPLOYEE BENEFIT PLANS

Goodwill has a defined contribution plan that covers substantially all of its full-time employees. The plan covers eligible employees who have completed one year of service, as defined in the plan, and have attained the age of 21. The IRS has determined that the plan is a qualified tax-exempt plan. Goodwill contributes, on a monthly basis, 5% of the first $25 of total eligible compensation and 8% of compensation thereafter to the plan. Participant contributions are not permitted under the plan agreement. Participants become 100% vested in Goodwill's contributions after three years of vesting service, as defined in the plan. During 2016 and 2015, Goodwill's contributions, net of forfeitures, to the plan were $4,225 and $3,908, respectively.

Goodwill has a 403(b) retirement plan that permits employees to defer a portion of their compensation, subject to annual IRS limitations. There were no employer contributions to the plan for the years ended December 31, 2016 and 2015.

Goodwill has a 457(b) tax-deferred compensation plan that is available to certain management employees. Participants may defer income into the plan on a pretax or post-tax basis, subject to annual IRS limitations. An asset and a liability of $550 and $465 are included on Goodwill's consolidated financial statements as of December 31, 2016 and 2015, respectively, within investments, other and other long-term liabilities.

NOTE L - CONTINGENCIES

Government contracts are subject to audit and adjustment by funding agencies. If government revenue is recorded for expenditures that are subsequently disallowed, Goodwill may be required to repay the questioned costs to the funding agency. Management of Goodwill is not aware of any disallowed expenditures that would have a material adverse effect on its consolidated financial statements.

Goodwill is involved in various legal proceedings, claims and administrative actions arising in the normal course of business. In the opinion of management, Goodwill's liability, if any, under any pending litigation or administrative proceeding will not materially affect its financial condition.

NOTE M - RELATED PARTIES

Certain members of Goodwill's board of directors are employed by various companies with which Goodwill does business.

Goodwill's operating revenue includes approximately $13 and $125 for 2016 and 2015, respectively, from companies with which certain Goodwill directors and management staff members are associated. Goodwill's purchased services and products include approximately $2,095 and $2,597 for 2016 and 2015, respectively, from companies with which certain Goodwill directors and management staff members are associated.

Contributions include donations received from Goodwill directors and management staff members, which totaled $148 and $98 for 2016 and 2015, respectively. Outstanding pledges from Goodwill directors and management staff members totaled $5 at December 31, 2016 and 2015.

NOTE N - DISCLOSURES ABOUT THE FAIR VALUE OF FINANCIAL INSTRUMENTS

The FASB accounting guidance on fair value measurement requires certain financial assets and liabilities be carried at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). Classification of the financial asset or liability within the fair value hierarchy is determined based on the lowest level input that is significant to the fair value measurement.

The guidance describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value. The following is a summary:

<u>Level 1</u> - Quoted prices in active markets for identical assets or liabilities.

<u>Level 2</u> - Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

<u>Level 3</u> - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The determination of where an asset or liability falls in the fair value hierarchy requires significant judgment. Goodwill evaluates its hierarchy disclosures each year and, based on various factors, it is possible that an asset or liability may be classified differently from year to year. However, Goodwill expects that changes in classifications between different levels will be rare.

(In thousands)

The following is a description of the valuation methodologies used for assets and liabilities measured at fair value. There have been no changes to the valuation methodologies used at December 31, 2016 and 2015.

Bond and stock mutual funds - Valued based on quoted market prices as of the date of the statement of financial position, as determined based on the market prices for the individual investments comprising each fund.

Derivative liability (interest rate swaps) - The fair value of Goodwill's interest rate swap agreements is based on estimates using standard pricing models as of the date of the consolidated statement of financial position. The fair value of the interest rate swaps is based on quotes from the counterparty of these instruments and represents the estimated amount that Goodwill would expect to receive or pay to terminate the agreements.

The carrying amount of Goodwill's financial instruments, which include trade accounts receivable, trade accounts payable and accrued liabilities, approximates their fair values at December 31, 2016 and 2015, due to their short maturities. The carrying value of long-term debt, including the current portion, approximates fair value because the interest rate approximates the current market rate of interest available to Goodwill.

The following table presents information about Goodwill's assets and liabilities measured at fair value as of December 31, 2016, and indicates the fair value hierarchy of the valuation techniques utilized by Goodwill to determine such fair value.

	Level 1	Level 2	Level 3	Total
Assets				
Bond and stock mutual funds	$550	$ -	$ -	$ 550
Liabilities				
Derivative liability, net (interest rate swaps)	-	1,466	-	1,466

The following table presents information about Goodwill's assets and liabilities measured at fair value as of December 31, 2015, and indicates the fair value hierarchy of the valuation techniques utilized by Goodwill to determine such fair value.

	Level 1	Level 2	Level 3	Total
Assets				
Bond and stock mutual funds	$465	$ -	$ -	$ 465
Liabilities				
Derivative liability, net (interest rate swaps)	-	1,993	-	1,993

NOTE O - SUBSEQUENT EVENTS

Goodwill evaluated its December 31, 2016, consolidated financial statements for subsequent events through June 14, 2017, the date the consolidated financial statements were available to be issued. Goodwill is not aware of any subsequent events that would require recognition or disclosure in the consolidated financial statements.